

REQUEST FOR PROPOSAL

FOCUSED AUDIT

ON

**THE AFFILIATED TRANSACTIONS BETWEEN
SOUTH JERSEY GAS COMPANY AND SOUTH JERSEY INDUSTRIES AND ITS
AFFILIATES**

PURSUANT TO

N.J.S.A. 48: 3-49, 48: 3-55, 48:3-56, 48:3-58 & N.J.A.C. 14:4-5 ET. SEQ.

AND

MANAGEMENT AUDIT

OF

SOUTH JERSEY GAS COMPANY

PURSUANT TO

N.J.S.A. 48: 2-16.4 & N.J.A.C. 14:3-12.1

DOCKET NO. AX04040277

**Division of Audits
New Jersey Board of Public Utilities
Two Gateway Center
Newark, New Jersey 07102**

SECTION 1 GENERAL INFORMATION

1.1 Introduction. On July 7, 2004, The New Jersey Board of Utilities (Board) initiated a Management Audit and a Focused Audit of South Jersey Gas Company (SJG, Utility or Company). SJG is a public utility under the regulation of this Board. SJG is engaged in the purchase, transmission, sale and transportation of natural gas for approximately 300,000 customers (residential, commercial and industrial) in an area of 2500 square miles. SJG's service territory includes 112 municipalities in Atlantic, Cape May, Cumberland, Salem and parts of Gloucester, Burlington and Camden counties. SJG also makes off-system sales of natural gas and capacity on a wholesale basis to various customers on the interstate pipeline system and transports natural gas purchased directly from producers or suppliers by some of its customers. SJG had two full comprehensive Management Audits performed on its internal workings and operations during 1984-1985 (Docket No. 849-1045) and during 1990 -1992 (Docket No. GA90030244). Also, during 1994 -1995, SJG had a Focused Audit performed on its existing gas supply needs and its gas supply strategies and capability for the future (Docket No. 94110526).

SJG is affiliated with four other companies [South Jersey Energy (SJE), South Jersey Resources Group (SJRG), Energy & Minerals, Inc. (EMI), and Marina Energy (Marina). All companies are subsidiaries of South Jersey Industries (SJI), and the four affiliates are not regulated by this Board. SJE is a licensed, deregulated energy supplier for residential, commercial, and industrial customers, offering energy management services, energy efficiency audits, lighting upgrades and retrofits, and energy efficient HVAC design and construction. SJE also sells natural gas to Atlantic City casinos and owns a 50 percent interest in AirLogics, LLC, which provides companies with a patented real-time environmental air monitoring system. SJRG, formed in 1996, is a wholly owned non-utility subsidiary of SJI and provides services for wholesale natural gas trading, sales, storage management, peaking services, transportation capacity and natural gas portfolio management. EMI principally manages liabilities associated with discounted operations of non-utility subsidiaries. Marina is in the business of developing energy-related projects in southern New Jersey, such as the development and operation of a thermal facility to provide for cooling, heating, hot water and electricity to the Borgata Resort (its largest client) in Atlantic City, New Jersey. SJI also has a joint venture investment with Conectiv Solutions, LLC, called Millennium Account Services, LLC (Millennium) that provides meter-reading services to SJG and Conectiv Power Delivery, the electricity provider in much of southern New Jersey.

This Request for Proposal ("RFP") establishes the guidelines for selecting a consulting firm (Contractor) to perform the audit. The Board is requiring the Contractor to submit a "not-to-exceed" bid in the proposal for this engagement. All costs related to this engagement will be borne by the Utility. Any additional work that is beyond the scope of the RFP must be presented to the Board for approval and the Contractor must satisfactorily demonstrate that it is directly related to this engagement before the additional payments are made by the Utility. Failure to meet the requirements of this RFP will be cause for rejection of any proposal. Acceptance of a draft contract between the Company and the Contractor is a required condition on being awarded this review.

1.2 Scope. This assignment will be developed in two phases. The first phase will be on a fast track and will concentrate on SJG's procurement strategies, and in particular the impact of transactions by and with affiliates of SJI, on a retail and wholesale basis. The Board

will expect a detailed examination of these transactions, specifically, at a minimum, gas procurement activities between SJG and SJI, the parent of SJG and/or other affiliates and other financial hedging and gas business transactions. This will also include a review and assessment of affiliate gas and capacity cost allocation methodologies to determine accounting and allocation procedures for separating costs of inter-company transactions. Additionally, the detailed examination will determine whether these accounting and allocation procedures are equitable and fair and do not favor certain affiliates over the utility and its ratepayers. Moreover, this phase should assess the gas commodity and capacity release and assignment strategies of SJG and its affiliates. This phase will be completed in two to three months from the signing of the contract, culminating with a Final Report on these transactions in the fall of 2004 that will have, where applicable, quantifiable Findings and Conclusions with supporting recommendations.

It should be noted that the Board, at its agenda meeting of June 23, 2004, directed Staff to revisit the findings and recommendations resulting from the previous competitive services audit (Dkt. No. GA02020101) during this audit. The previous audit, performed by Overland Consulting, Inc., covered the period from September 2002 to December 2002. It is expected that the prospective consultant review Overland's entire report and comment on whether any or all of these recommendations should be accepted by the Board.

The second phase will focus on all other aspects of the Utility, as discussed below and will include the organizational structure of SJG, its financial controls, financial integrity, and corporate accountability. This examination will also concentrate on the adequacy of the separations of functions within the SJG operations for its competitive services and all transactions between SJG, SJI and the other affiliates to assure that SJG customers are not supporting the activities of its affiliates and its parent and that SJG has not been exposed to risks associated with its affiliates.. Also, this phase incorporates all of the requirements that are part of the Electric Discount Energy Competition Act ("EDECA") as specified in N.J.S.A. 48:3-49, N.J.S.A. 48:3-55, N.J.S.A. 48:3-56, N.J.S.A. 48:3-58 and N.J.A.C. 14:4-5 et. seq. The Board will expect a detailed examination of these transactions regarding internal financial controls, financial integrity, corporate accountability and the standards of conduct applicable to these transactions.

The two phases of the audit should give an insight into the philosophy and direction of SJG, SJI and its affiliates as follows:

- ? Documentation of Affiliate Relationships – The policies and procedures that define the need, necessity, legal entitlement and the nature of the relationship between affiliates.
- ? Cost Allocation Methodologies – The cost allocation methods among SJG, SJI and its affiliates. Whether they are the result of arms-length negotiations and whether they, as much as possible, allocated costs on a direct assignment basis. If this was the case, explain the rationale for these allocation methods and make appropriate recommendations.
- ? Price of Goods and Services – Review whether the pricing of SJG goods and

services to and from SJI and its affiliates is appropriate, non-discriminatory and does not exceed market rates.

- ? Effect of Affiliate Relationships – Examine whether the holding company structure and the affiliates, along with their diversified activities have had or may have any detrimental effect on SJG.
- ? Internal Controls – Examine whether SJG has an internal system to provide reasonable assurance that its goals and objectives are accomplished at the lowest possible cost to its ratepayers with the maximum benefit to its customers. The internal controls should give a true and accurate account of the transactions of SJG and its affiliates and should show that the transactions have been carried out with integrity and according to appropriate standards consistent with regulatory and legal requirements and standards. Examine whether SJG has an internal control that protects against irregular, illegal, and/or improper transactions, including accounting and financial activities that could result in trading irregularities, market price manipulation, false price information or unfair capacity and gas cost allocations from SJI or any of its affiliates to SJG.
- ? Corporate Governance – Review the corporate structure and whether the Board of Directors and senior management are able to anticipate and respond to strategic issues on an ongoing basis by assuring that the stockholders, as well as the ratepayers, are insulated as much as possible from financial harm. Determine whether the Board of Directors has the experience and knowledge to fulfill the corporate goals and objectives and ensure that no director has any conflicts of interest or self-interest or unreasonable influence while sitting on the Board.
- ? Capacity Allocation SJG allocation of the costs of the Company's design day resources to any particular customer class or classes. How does SJG hold an "open season" for capacity assignment to LVS customers?

PHASE ONE

Focused Audit of Affiliated Transactions

This phase involves the financial and business interactions of SJG and SJI and the other affiliates. The Contractor must address, at a minimum, the following areas:

GAS PROCUREMENT ACTIVITIES

A complete review of gas procurement activities shall be included in the consultant's work scope, as follows:

- a. Define, document and support all gas procurement activities from the last eight years and evaluate their effectiveness in procuring the best possible gas prices to SJG's customers.
- b. Identify the strategy for gas procurement to SJG over the last eight years.

- c. Determine supply reliability and identify any problems that caused financial harm to the ratepayers over the last eight years.
- d. Identify SJG's spot market philosophy and define the best price mix between price and reliability over the last eight years.
- e. Identify SJG's overall gas commodity purchasing philosophy and define the best price mix between price and reliability over the last eight years.
- f. Identify SJG's interstate pipeline capacity purchasing philosophy and the amount of interstate pipeline capacity it must maintain at any given time and define the best mix between price and reliability over the last eight years.
- g. Review all contracts between SJG and the other affiliates and SJI over the last eight years.
- h. Determine appropriate gas supply, including capacity and whether the Company's purchases are and have been allocated appropriately among customer classes over the last eight years.
- i. Determine whether all purchases occurred in a competitive market and whether SJG received the best possible price for its gas.
- j. Evaluate the purchasing department's independence in purchasing supplies on behalf of SJG from the highest management /officers to the lowest level of staff and define whether it acted in the best interest of SJG ratepayers over the last eight years.
- k. Evaluate the interrelationship among SJG and SJRG and whether SJRG's internal controls and structure allowed for them to make purchases on behalf of SJG in a manner that was in the best interest of SJG and its ratepayers over the last eight years.
- l. Examine and document the level of activity with regard to customers transferring to third party suppliers during the last eight years, including an examination of the competitiveness of the TPS' market in SJG's service territory. Provide suggestions on ways to improve on the competitiveness of the TPS market in the SJG territory.
- m. Evaluate internal controls and the flow of information between SJG and its affiliates with regard to gas purchases.
- n. Evaluate all correspondence between all directors and officers in the area of Gas Procurement Activities to determine whether there were arms-length discussions, to ensure compliance with the affiliate relationship and fair competition standards, and to determine whether SJG ratepayer's interests were harmed.
- o. Provide findings and recommendations and suggested solutions to correcting any problems uncovered through this audit.

- p. Review SJG's strategy and philosophy of undercutting BGSS by 5% and its effect on pricing and refunds and other relevant areas for the past eight years.
- q. Evaluate all commodity and capacity release and assignment transactions made by SJG and/or its affiliates over the last eight years and determine whether they were performed in the best interest of its ratepayers. Also evaluate their impact on competition in the SJG service territory.

REVIEW AND ASSESS AFFILIATE COST ALLOCATION METHODOLOGIES

- a. Determine the accounting and allocation procedures for separating costs of inter-company transactions of SJG with affiliates.
- b. Determine if the joint/common costs are properly allocated between SJG, SJI and its affiliates and if not, calculate the appropriate costs.. Provide, as much as possible, direct cost allocation.
- c. Review the practices of time sheet reporting by employees with shared SJG/SJI responsibilities to determine appropriate allocations.
- d. Determine if the duties and responsibilities of employees who bill time for SJG, SJI and/or its affiliates are at cross-subsidization purposes.
- e. Evaluate affiliate cost allocation methodologies for adherence to applicable legal, regulatory and contractual requirements.
- f. Evaluate affiliate charges and cost allocation methodologies among SJG, SJI and its affiliates.
- g. Review and assess pricing policies between affiliate interests, i.e., market price of gas as compared to cost of purchased gas by SJG or SJE.
- h. Review and assess bidding procedure policies and procedures that are done in a competitive or non-competitive manner.
- i. Identify all lease arrangements between SJG, SJI and its affiliates, and determine whether their terms are consistent with the competing local markets and the costs are allocated appropriately.

PHASE TWO

The second phase will consist of a comprehensive audit of SJI and SJG's other major organizational areas and functional processes, procedures and internal workings. This will include Executive Management and Corporate Governance, Strategic Planning, Finance, Accounting and Property Records, Distribution and Operation Management, Human Resources, Customer Services, External Relations and Support Services. This phase should include, at a minimum, the following areas:

EXECUTIVE MANAGEMENT AND CORPORATE GOVERNANCE

A complete review of executive management and corporate governance issues shall be included as part of the consultant's work scope, as follows:

- a. Selection of directors for the holding company and the utility
- b. Independence of auditors;
- c. Committee structures;
- d. Separation of the Chairman and Chief Executive Officer titles;
- e. Compliance with the Sarbanes-Oxley Act;
- f. Compliance with NYSE requirements;
- g. Executive Compensation – Review the issue of executive compensations including a comparison with other New Jersey utilities;
- h. Relationships between affiliates; compliance with affiliate relation rules and the effect of FERC rules.
- i. Review of any lawsuits that have been brought before the Company's Board of Directors or its officers.
- j. Examine SJG's senior management's independence relative to its own performance and best interest of its ratepayers.

ORGANIZATIONAL STRUCTURE

- a. Assess the resources allocated to SJG versus non-regulated activities of SJG, SJI and its affiliates.
- b. Identify policies and procedures for adherence to applicable legal, regulatory and contractual requirements.
- ? Review adherence by SJG, SJI and its affiliates to these policies and procedures.

- ? Review and assess these policies and procedures as to how they affect SJG, SJI and its affiliates.
- c. Review and assess affiliated interest contracts to determine if they are strictly “at arms length” and appropriate in light of current market conditions, without cross-subsidization.
- d. Determine the portion of gas sales by SJI and its affiliates to SJG and the relative dependence on these sales to continue as a “going concern,” without cross-subsidization.
- e. Review and assess internal controls to determine their effectiveness and independence.

STRATEGIC PLANNING

a. Organization, Purpose and Mission

- ? Review and assess how well the purpose and mission of the organization is defined.

b. Goals and Objectives

- ? Define the specific short and long range goals of each affiliate.

c. Business Strategy

- ? Review of business strategy for impact of business and financial risk to SJG.
- ? Review and assess how strategic plans are developed.

d. Implementing and Executing the Strategic Plan

Examine commitments and resources for implementing the strategic plan.

e. Evaluating and reformulating the Strategic Plan in light of actual experience, changing conditions and priorities

- ? Does the corporate plan contain essential elements to provide overall direction to SJG (i.e., including key assumptions and the basis for resource allocation)?

- ? Is the planning responsive to changing conditions? Are planning components adequately addressed (i.e., including key business functions, SJG assessment, the environmental assessment, customer impact and the competitive assessment)?
 - ? Is the plan communicated effectively as to employee awareness and linkage to the annual budget (reflecting consistent goals, objectives, and financial performance targets)?
- f. Is the management of SJG focused on itself or elsewhere?
- g. Is the expertise of SJG being diverted to SJI and its affiliates?
- h. Are the goals of SJG in conflict with those of the SJI and its affiliates? If so, provide details and how it can be mitigated or diminished.
- i. Has diversification caused harm to SJG and, if so, how should such harm be corrected?
- j. Are SJG's goals, as they exist today, appropriate in today's industry environment, or should they be changed? What would be appropriate goals?

FINANCE

General Overview

- a. Complete review of all financing of SJG and SJI and all affiliates to determine the extent to which SJG may have been directly or indirectly affected.
- b. Review and assess financial performance of SJG, SJI and its affiliates and the financial effect that this affiliate interrelationship has on the individual company financial performances.
- c. Assess the exposure of SJG's credit quality as a result of the activities of SJI and its affiliates.
- d. Review the amount of stress on the financial integrity of SJG and quantify the effect.

Financing

- a. Review the debt management for SJG, SJI and all affiliates.
 - i. Identify any real or perceived encumbrance of utility assets for non-utility purposes.
 - ii. Complete review of all external financings by SJG to determine the extent of any negative effects from the diversified businesses.

- b. With respect to SJG, SJI and its affiliates' investment decisions, assess the degree to which tax considerations may have outweighed other investment criteria (i.e., safety) in deciding what investments to make, and assess the effects of SJI's financings on SJG.
- c. With respect to the determination of consolidated income taxes for SJG, SJI and its affiliates, review and clearly set forth the method and principles underlying the determination, and the allocation of the taxes to the affiliates:
 - i. SJG current treatment; prior rate case treatment reflected in Board decisions over the past 8 years;
 - ii. Other treatments allowed by the IRS, if any; and
 - iii. Advantages and disadvantages of each and equity of each.
- d. Assess the degree to which the historical and projected tax benefits from diversified activities have been and are projected to be realized as a result of the taxable income of SJG, and provide the identity of the chief beneficiaries.

Cash Management

- a. Evaluate the cash forecasting and diversification of investments between all levels of management.
 - ? Explain in detail the cash management of SJG, SJI and its affiliates and determine whether SJG is separate from the others.
 - ? Determine the extent of the use of funds generated from the Utility's depreciation for non-utility purposes. Make recommendations, if appropriate.
- b. Determine if the use of SJG's generated income by SJI and its affiliates represents a drain on SJG financing ability or value – either by affecting dividend policy, retained earnings, cash flows or other financial parameters.
- c. Identify and quantify specific instances of major write-offs or the likelihood of same by SJG, SJI and its affiliates, and the potential financial impact on SJG.
- d. Determine if the cost of capital to SJG has increased due to increased risk associated with diversifying activities.
- e. Review and assess the cost of capital to SJG relative to the cost of capital to utilities of comparable risk but without non-utility affiliates.
- f. Provide definitive recommendations to insulate SJG's capital costs from non-utility operations.

ACCOUNTING AND PROPERTY RECORDS

a. Accounts payable

- ? Evaluate the processing, recording, authorization and accountability of the accounts payable function between all levels.

b. Accounts Receivable

- ? Review how payments are received, processed and secured between levels.

c. Compensation and benefits

- ? Review the independence, processing, security and accountability of the payroll function, including employees' time and effort associated with payroll. Determine the reasonableness of the executive compensation package of SJG, SJI and its affiliates and detail the basis and reasonableness for the allocation of these costs to SJG.

d. Budgeting

- ? Evaluate budget reporting, tracking, revision and analysis at all levels.

e. Work Order Procedures and Continuing Property Records

- ? Evaluate work order procedures at all levels.

f. Capacity Assignment Issues

This methodology should determine the specific amounts, and the specific pipeline or pipelines subject to the "open season" for all of its customers.

The notice of the open season will specify:

Quantities of capacity available;
Pipelines on which the capacity is available;
Renewal and recall rights applicable to the capacity.

What customers may also acquire capacity from the Company outside of the "open season?"

Will all capacity assignment be subject to margin sharing?

Is there a methodology to make "virtual" storage available to LVS customers who receive pipeline capacity during the "open season?"

How does a capacity assignment from the "open season" become eligible for two (2)

consecutive renewals, after which capacity will be returned to the Company's portfolio, and the LVS customers who had received the capacity assignment may then participate in an "open season?"

Review the terms of the current two LVS customers receiving capacity assignment that is allocated to their existing capacity simultaneously with the first "open season."

Review SJG portfolio mix of its interstate pipeline capacity, and "virtual" interstate storage capacity to marketers.

Review the capacity that is assigned based upon the requirements of residential and C&I customers served by the marketer.

How would marketers to whom pipeline capacity is assigned be restricted from remarketing pipeline capacity? Will storage capacity assigned be "virtual capacity" and not be remarketed?

How will SJG assign pipeline and storage capacity subject to recall rights or termination of SJG's design day forecast or other operating conditions require South Jersey's to exercise such rights?

Other Relevant Concerns

The above RFP reflects current areas of concern, especially in corporate governance and relationships of affiliates. At the RFP conference and during the pre-audit and audit phase, the Board Staff may advise the Contractor of items that may not be explicitly identified above but may be directly related to the audit. Whenever this occurs, the Contractor must include that item(s) in the investigation, and it is considered within the scope.

1.3 Objective. The ongoing evolution of business practices and legal frameworks since the deregulation of the energy markets has permitted diversification into non-utility, non-regulated lines of business of the Company. The concern of regulators is that the risks of diversification should be borne by shareholders and not ratepayers of the regulated Utility. The results of this audit will assist the Board in determining: (1) if the operation of the Company and/or any unregulated affiliate have adversely impacted upon the financial integrity and/or financing capability and/or flexibility of the Utility; (2) if the rates paid by the utility's customers were being used to subsidize the operations of the unregulated businesses; (3) if transactions between the Company and/or the affiliates and the Utility are at arms length; (4) if resources are adequately and appropriately allocated to insure that the mission of the regulated entity will be to continue to provide safe, adequate and proper service at a reasonable cost and the mission is achievable; and (5) if the gas procurement activities between SJG, SJI and its other affiliates are at arms length and if SJG is procuring its gas supplies at the most reasonable and prudent costs. The audit should be comprehensive enough to allow for assessment of the issues and opinion on the feasibility of the continuation of the present structure of SJG and the effect the parent, SJI and the other affiliates have on SJG's performance in providing safe,

adequate and proper service and receiving its gas in proper manner in accordance with the rules of fair standards in the gas trading arenas.

1.4 Schedule. It is the Board's intention to adhere to the schedule for this Audit as set forth in Attachment 1.

1.5 Definitions and Responsibilities of Parties. The definitions and general responsibilities of the Board, Utility, and Contractor are as follows:

1.6 Board. The Board is the client for whom the audits are to be performed and is the sole point of contact for this RFP. The Board its Staff ("Staff") will: (1) evaluate the submitted proposals; (2) choose the Contractor; (3) supervise the performance of the audits; (4) review the Contractor's expenses and authorize payment by South Jersey Gas Company; and (5) utilize the results of the audits for the purposes set forth in the RFP.

1.7 Utility. SJG, the Utility is the subject of the audit and will be the signatory to the contract. The Utility will: (1) be responsible for all costs related to this audit; (2) cooperate with the Contractor and Staff; (3) provide timely and complete responses to all document and interview requests; (4) provide adequate working space and necessary office equipment for the Contractor and Staff; and (5) shall have the right to contest the methodology and rebut the findings of the audit along with identifying any factual discrepancies in the Contractor's reports(s).

1.8 Contractor. The Contractor is the selected consulting firm(s), its personnel, and subcontractors. The Contractor will: (1) perform the audit(s) under the supervision of Staff; (2) ensure that any subcontractors comply with the RFP; (3) report, as required, to Staff; (4) submit expenses to Staff for the authorization of payment; (5) notify Staff immediately if utility or its affiliates are not responding expeditiously or adequately to consultant's inquiries; (6) notify Staff of any matter it feels is not in accordance with the RFP or the subsequent contract; (7) advise Staff when its budget for this assignment is 75% exhausted with an explanation and justification if it feels that the projected work will exceed the budgeted amount; (8) submit the results of the audit(s) to Staff; and (9) provide testimony, if required, regarding the results of the audit(s). The Contractor will adhere to a Code of Professional Conduct in its relationship and interactions with the utility, the Board or its Staff or any other interested party during this assignment. The Contractor will treat all information as confidential and will neither take personal advantage of privileged information gathered during the assignment nor enable others to do so. The Contractor will neither accept commissions, remunerations other than the compensation provided by the contract to be entered in this matter, invitations to events, luncheons, dinners or other benefits in connection with this assignment without the knowledge and consent of the Board or its Staff, nor fail to disclose any financial interest in goods or services which form part of the audit. The Contractor shall have no interest, nor promise to acquire any interest, direct or indirect, which would conflict in any manner or degree with the performance of its services hereunder. The Contractor will agree that, in the performance of this assignment, it shall knowingly not employ any person having such an interest. The Contractor further certifies that no member of the board of the Contractor or any of its officers or of its subcontractors has such an adverse interest. The Contractor will insure that before this assignment is accepted and during this assignment that any personal, financial or other interest which might influence the conduct of the assignment be disclosed. The Contractor will

advise Staff if any promise of employment is offered by the utility to the Contractor during this assignment.

1.9 Confidentiality. It is anticipated that after the Board has selected the winning bidder, all proposals filed by the contractors and a copy of the contract will be available for public inspection, unless otherwise ordered by the Board. Any prospective contractor (bidder) who wishes to claim confidentiality for any portion of the RFP submission must follow the procedures set forth in the N.J.A.C. 14: 1-12, a copy of which is available on the Board's website at www.bpu.state.nj.us.

1.10 Rejection of Proposals. The Board reserves the right to reject any or all submitted proposals not in conformity with this RFP, or for any other cause deemed appropriate after consultation with the Commissioners.

1.11 Proposal. Prospective contractors ("bidders") must submit a complete response to this RFP. It should be addressed to: Walter P. Szymanski, Director of Audits, Two Gateway Center, Newark, NJ 07102. Also, an RFP Review Conference will be held at the Board's Newark office in order to respond to any bidder questions on the RFP and further explain the purposes of this engagement. There must be one original proposal, signed by an official authorized to bind the bidder to its provisions, and 10 copies, along with one reproducible copy for Staff to make additional copies if necessary. The proposal must remain valid for the length of the audit(s). The proposal must state the intention to accept all conditions of the contract or explain the reasons why that acceptance cannot be made. Once all accepted proposals are reviewed, Staff may require interviews with the remaining bidders to discuss the contents of the proposals. Both the RFP and the proposal will comprise contractual obligations for the selected Contractor(s), unless modified by mutual consent.

1.12 Incurred Costs. Neither the Board, the Staff, nor the Company shall be liable for any costs incurred by the Contractor prior to the Board's authorization to execute a written agreement signed by the Utility and the Contractor. Also, any person not listed in the Contractor's proposal will not be reimbursed for their work in performing this assignment, unless specifically approved, in writing, from the Board or its Staff.

1.13 Compensation. Payment of any contractual costs incurred subsequent to the signing and authorization of a written agreement will be made upon receipt of the Contractor's invoice, as set forth in Section 3.4. Payment of monthly invoices will be 100% of the undisputed amount of expenses and 80% of the undisputed amount of professional and support staff fees. The remaining 20% will be paid when the Board accepts the final report and all contractual obligations have been met. Disputed amounts shall be subject to and brought before the Board for resolution.

SECTION 2 PROPOSAL CRITERIA

The review and evaluation of your proposal will be based upon the following format:

2.1 Summary. A discussion reflecting the bidder's understanding of the proposed audit.

2.2 Work Plan. A discussion setting forth the bidder's work plan, as follows:

- A. Approach, with emphasis upon the techniques for collecting and analyzing data;
- B. Products to be delivered and time estimates for each task;
- C. Sequence and relationship of all areas to the experience of the personnel in each category; and
- D. Methods of managing the work to be performed.

2.3 Experience. A resume of the bidder must be provided indicating previous experience relating to this engagement, with full identification of all references and descriptions of assignments completed and their pertinence to this engagement.

2.4 Personnel. Resumes of all personnel to be involved in the audit(s), must be provided, including previous relevant experience, clients served, and respective dates. Experience that does not reflect previous work assignments as it relates to the assignment may not be considered for evaluation. There needs to be a sufficient number of high-level experienced personnel. The Board's Director of Audits must approve any substitution of personnel during the assignment after a review of the bidder's written justification; including detailed resumes of the substitute personnel.

2.5 Relationship with the Utility, the Parent, and/or its Affiliates. A detailed statement indicates any prior, existing, or prospective relationship, financial or otherwise, between the Contractor, its personnel, and/or subcontractors, and the Utility, the Parent, or its affiliates being audited.

2.6 Costs. List separately the estimated costs for services, itemized as follows:

- A. Professional and support staff fees of all personnel, consisting of the projected hours and rate per hour for each category;
- B. Supplies and materials;
- C. All travel expenses, including transportation, meals, lodging, etc.; and
- D. Any other direct costs;
- E. Costs incurred after completion of the written audit, if necessary for the

presentation of findings, e.g., cross examinations, hearings, and all other procedural matters, will be in addition to the cost of the audit(s). These costs will be borne by the affected company (ies); and

- F. Costs for the performance of work determined to be outside the initial scope of the RFP will be only incurred after specific, written authorization of Staff. The hours worked shall be billed at the professional rate per hour, based upon all professional rate categories set forth in Section 2.1.6. If Staff determines additional hours to be necessary, said hours shall be considered to be a modification of the written agreement and shall be mutually agreed upon by Staff and the Contractor, subject to approval by the Board.

2.7 Other Information. Any other information that may assist in the review of a submitted proposal, such as brochures, literature, or samples of recent assignments completed, may be submitted with, but shall not be considered part of, the proposal. The Board may award a contract for any or all parts listed under the Scope.

2.8 Evaluation Criteria. The criteria and the percentages of their importance in making the selection are as follows:

- A. Understanding the RFP and Work Plan (35%) This refers to the technical soundness or the Contractor's stated approach to the project, the comprehensiveness of the proposed approach, and the techniques to be used. A determination will be made regarding the Contractor's understanding of the project purpose and goals as presented in the RFP. Evaluation will be based on the data presented in the consultant proposal, and the approach and allocation of time on specific tasks. Contractors should feel free to suggest other requirements and problems not referenced herein. The Board Staff will evaluate the clarity and adequacy of the detailed project plan and the ability to adhere to the assignment and meet the schedule.
- B. Personnel Qualifications: (30%) Board Staff will evaluate the ability of prospective Contractor to meet the terms of the RFP relative to having a consulting team with the qualifications needed to successfully complete the project. Qualifications of professional personnel assigned to the project, as specified in the proposal, including subcontractors, will be experience on projects similar to that described in the scope of work. The Contractor's professional and project staff that work on the project must be the same staff identified in the proposal. The Board's Staff must approve subcontractors.
- C. Overall Evaluation and Innovativeness: (5%) This RFP generally outlines the work activities and products expected by The Board. A factor in the selection of a firm, in addition to terms in A through B above, is any innovative approach that goes beyond the suggested scope of work. It must be shown how this will be accomplished within the time limits and how it is related to the scope and objectives of the assignment. The scope should be broadly construed.

- D. **Firm's Experience: (15%)** This covers the prospective Contractor's experience working as a cooperative team with other contractors and public agencies. Qualifications of professionals assigned will be measured by experience on past projects within a cooperative team environment.
- E. **Cost: (15%)** The proposal will be evaluated on the overall cost of the assignment, including the hours, number of personnel assigned, direct and indirect costs, restrictions stated or implied in the proposal and travel concerns during the assignment. Consideration for cost will concern how the quality of the proposal relates to the costs of the assignment in order that the Board receives the best possible contractor at the lowest possible cost.

SECTION 3 AUDIT PROCEDURE

3.1 Safety Standards. On the Utility's premises, the Contractor must comply with all regulatory standards and Utility policies dealing with safety, insurance, and work specifications.

3.2 Project Control. The audit(s) will be performed in accordance with the RFP and the written agreement between the Contractor and the Company. The Contractor will directly report to the Board or Audit and Energy Staff, as directed by the Project Manager. All written and oral communications will be through Staff's Project Manager, unless there is a need to communicate immediately, in which case, Staff's Project Manager will be notified as soon as possible. The Contractor may be requested to discuss audit progress with Staff, as necessary.

3.3 Monthly Progress Reports. The Contractor shall submit a written monthly report to the Project Manager and to the Energy Division for any month in which work was performed. The report shall consist of a general narrative providing adequate and detailed information regarding the status of the audit(s), with an explanation of any discrepancies between the approved work plan and actual progress. A Gantt chart will be provided with each monthly report.

3.4 Invoices. All invoices shall be presented to Staff with the Monthly Progress Reports and supported by appropriate documentation and may be subjected to an audit by the Board and/or the Utility for a period of two years after the completion of the audit(s). The invoices should be itemized as in Section 2.1.6 and shown in relation to the contractual cost.

3.5 Draft Report(s). A draft report(s) shall be submitted to Board's Staff and shall include a summary of the audit process and a summary of all recommendations. After appropriate review and authorization by Staff, the Contractor will release the draft report (s) to the appropriate company(ies) for review, limited to identification of factual discrepancies. Afterwards, Staff will authorize the preparation of the Final Report(s). The Utility will be permitted to comment on the Contractor's findings and recommendations after the Board or its Staff releases the final report. These comments will be a separate correspondence and not made a part of the Contractor's report.

3.6 Final Report(s). The Contractor shall provide a maximum of 25 bound copies of the Final Report to be filed with the Board and one master copy suitable for photocopying, or as

Staff may deem appropriate and also electronic copy to the Staff Project Manager and the Energy Division. The Board may authorize the printing of a number of Redacted Final Reports to protect proprietary information, if necessary. The Final Report(s) will only be released upon authorization from the Board.

ATTACHMENT 1

FOCUSED AUDIT ESTIMATED SCHEDULE

- | | |
|---|-------------------|
| 1. Send RFP to prospective contractors | July 9, 2004 |
| 2. Receive letters of intent from bidders | July 16, 2004 |
| 3. RFP review conference | July 20, 2004 |
| 4. Receive proposals from bidders | August 2, 2004 |
| 5. Board selects Contractor | September 8, 2004 |
| 6. Signing of contract | September 8, 2004 |
| 7. Audit begins | September 9, 2004 |
| 8. Contractor submits draft report | December 13, 2004 |
| 9. Staff releases draft report to utility | December 20, 2004 |
| 10. Utility submits comments on factual accuracy and
Proprietary information on the draft report | January 10, 2005 |
| 11. Exit Meeting | January 14, 2005 |
| 12. Contractor files final report | January 24, 2005 |
| 13. Utility submits comments on findings and recommendations | January 31, 2005 |

? **The above are Estimated Dates and may vary based upon direction from the Board.**

ATTACHMENT 2

MANAGEMENT AUDIT ESTIMATED SCHEDULE

- | | |
|---|-------------------|
| 1. Send RFP to prospective contractors | July 9 2004 |
| 2. Receive letters of intent from bidders | July 16,2004 |
| 3. RFP review conference | July 20, 2004 |
| 4. Receive proposals from bidders | August 2, 2004 |
| 5. Board selects Contractor | September 8, 2004 |
| 6. Signing of contract | September 8, 2004 |
| 7. Audit begins | September 9, 2004 |
| 8. Contractor submits draft report | February 7, 2005 |
| 9. Staff releases draft report to utility | February 14, 2005 |
| 10. Utility submits comments on factual accuracy and
proprietary information on the draft report | February 21, 2005 |
| 11. Exit Meeting | February 25, 2005 |
| 12. Contractor files final report | March 7, 2005 |
| 13. Utility submits comments on findings and recommendations | March 14, 2005 |

? **The above are Estimated Dates and may vary based upon direction from the Board.**